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SUBJECT: PERU: LABOR REFORM INCHES FORWARD

Peru: Labor Reform Inches Forward

1. (SBU) Summary: In seeking consensus on the General Labor Law, the congressional labor committee plans to consult again with civil society before it submits a draft to the plenary. Continued political differences over specific issues -- particularly the rights of dismissed workers and the right to sector-wide collective bargaining -- suggest the bill will face an uphill battle, and potentially stall there. Critics of the bill, which would only apply to the 25 per cent of the Peruvian workforce in the formal sector, claim that it would impose rigid labor conditions at a time when the Peruvian economy desperately needs to create more jobs. President Garcia and PM Del Castillo have stated they would veto any bill that fails to strike the proper balance between business and labor. Meantime, the GOP is moving to institute other measures that would apply to a broader group of Peruvian workers who remain outside the formal sector, providing them for the first time with basic labor rights and social benefits. End Summary.

Elusive Consensus

2. (SBU) Congress's labor committee continues seeking an elusive consensus on the contentious General Labor Law. Progress on the bill broke down in December when congressman Luis Negreiros of the ruling APRA party sought changes to Article 165 to restrict companies' ability to fire their employees. A chorus of business groups and pro-growth political leaders, including government officials, complained that the proposed changes returned Peru to an era of labor rigidity that made it impossible, in practice, to get rid of employees without incurring exorbitant penalties. Negreiros has since backed down, but the issue remains unresolved. A second impasse emerged over Article 364, which requires unions to obtain the consent of businesses before engaging in sector-wide bargaining. According to congressional staffers, Negreiros and others who wanted to facilitate sector-wide union organizing were overruled by congressmen focused on the growth (including of formal employment) side of the equation. This issue too remains unresolved. Articles relating to subcontracting remained essentially unchanged from December, when the committee tightened the obligations of primary employers to ensure subcontractors shared in the profits of companies.

¶3. (SBU) Minister of Labor Susanna Pinilla acknowledged in a January 24 meeting with Emboffs that key elements of the labor law remained under contention, and the prospect of a quick resolution was unlikely. She averred that, notwithstanding the Ministry's persistent and painstaking explanations, key members of the labor committee were still convinced that the best way to improve the lot of workers was to enact inflexible labor standards, reminiscent of those that preceded Peru's economic crises in the 1980s. For their part, business groups and their congressional allies have kept up a steady drumbeat of complaints, warning that new labor protections in Peru--already among the toughest in the region--will choke off foreign investment and increase unemployment. Ministry of the Economy officials were sympathetic to this view in a January 24 meeting with Emboffs and suggested the final law, whatever form it takes, could decrease formal employment by raising labor costs. Critics of the law, including key government officials, have made precisely that point, noting that the bill only covers the roughly 25 per cent of the labor force in the formal economy.

¶4. (SBU) Labor Minister Pinilla told us that, when the new congressional session opens in March, the labor committee planned to invite civil society, labor and private sector representatives to review and comment on the work done up to now -- a process that could take several months. Pinilla and other insiders have speculated that, at the end of the day, the committee could deliver a bill to the plenary without having resolved these thorny outstanding issues beforehand. This suggests that the bill will face tough sailing in the plenary, and could even stall there -- a possibility that Pinilla openly acknowledged. Moreover, President Garcia said he would veto any law that tilted excessively toward either business or labor. To cover his social sector flanks, Garcia reportedly told International Labor Organization's (ILO) Director-General Juan Somavia in Lima last week that the GOP was committed to do "everything necessary" to improve working conditions, raise wages, and increase social benefits. Tacking in the other direction, Prime Minister Del Castillo stated January 25 that the government would block, and return to sender, any version of the bill that threatened economic growth or the expansion of jobs in the formal labor sector.

A Complementary Approach

¶5. (SBU) To complement their work on the labor law and to begin to tackle the real labor problems besetting Peru, the government has issued decrees and prepared additional legislation to strengthen labor protections more broadly, and to attempt to attract workers into the formal sector. In reviewing this strategy, Minister Pinilla told us:

- The government created an interagency committee to combat forced labor in January and plans to issue an action plan within 30 days;
- In March, the GOE will implement its new "Salud y Seguridad en el Trabajo" Law (Safety in the Workplace Law);
- In October 2006, the GOP issued Law 28806, which doubled the number of labor inspectors to more than 500, and increased their authority to conduct unannounced inspections and levy fines. The government plans to redouble the number of inspectors in 2007; and
- The GOP also has begun a process of judicial reform to streamline procedures for resolving time-consuming labor disputes.

¶6. (SBU) The Ministries of Economy and of Labor also are quietly modifying legislation affecting small business to encourage more micro-enterprises (business with less than 10 employees) to enter the formal sector. (More than 90 per cent of Peruvian business are micro-enterprises, and approximately 55 per cent of the work force is in small business.) In particular, proposed changes reduce the paperwork needed to set up and maintain small businesses, lower tax rates, and offer workers the opportunity to participate in the system of social benefits provided by the

government, such as pension rights, paid vacations, severance pay and health insurance. Minister Pinilla told us this legislation would seek to create an "intermediate step" between informality and the comprehensive rights and benefits package enjoyed by the small minority of workers in the formal sector, and explained that the government sought to bring some benefits to those who had nothing while avoiding undermining the rights of those who already had them.

17. (SBU) Comment: The proposed General Labor Law remains a problematic work in progress. In any case, it represents only one part of a comprehensive GOP plan to improve labor rights and benefits. The law itself, if passed, would provide some new benefits to the minority formal sector. But other GOP proposals are designed to tackle some of the most intractable problems that Peru's economy faces: how to reduce the country's large informal sector and introduce basic social benefits and labor rights to the majority of the workforce. The Garcia administration is proceeding in keeping with its rhetoric, hoping to balance economic growth and incentives with social justice. That said, the Garcia administration has increased the pace of change in part to help win passage of the Peru Trade Promotion Agreement (PTPA), but also in response to the social and political costs of a labor force that remains largely outside the law. End Comment.
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